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**Cotton, Norton, Stevens
Consulting, Inc.**



Telephone: (602) 954-8812
Facsimile: (602) 954-8908

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Mr. Jim Fisher, Executive Consultant
Arizona Corporation Commission - Utilities Division
1200 West Washington St.
Phoenix, AZ 85007

W-04254A-04-0270
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RE: 'Montezuma Estates Property Owners' Association (MEPOA) scheduled ACC hearing of October 28, 2004 to Sell Its Assets and Transfer It's Certificate of Convenience and Necessity to Montezuma Rimrock Water Company (MRWC).

Dear Mr. Fisher:

ACC's oversight of the application and ultimate approval of the party that is approved to purchase MEPOA's water system is an important matter to the residents, property owners, and investors in the MEPOA service area. The Commission has treated it as an important matter and in the July 8th hearing expressed a concern about the financial capabilities of the applicant and continued the hearing. **From a property owner's standpoint the financial stability and related operating capacity of the prospective buyer is particularly important in (A) Resolving concerns relating to the present available water supply for MEPOA's service area, and (B) Meeting the new arsenic level regulations which become effective in January, 2006. These two matters as well as the effectiveness of MEPOA's Board in seeking out qualified buyers are discussed below. Sources for the information presented are a review of the transcript of the July 8, 2004 hearing on this matter and experience gained as a result of being a property owner in the service area.**

As to water supply MEPOA has 2 wells operating. Well #1 is pumping 35 GPM & Well #2 operates at 12 GPM for a total pumping rate of 47 GPM. In recent years, Well #2 has been reworked at an approximate cost of \$22,000, however the well will still occasionally pump dry. This pumping rate is basically one half of what existed in 1999 when Well #1 was equipped for 88 GPM and Well # 2 was at 16 GPM for a total pumping rate of 104 GPM. Possible causes for the decrease in MEPOA's pumping rates include (a) the additional wells drilled to serve the residences being constructed in the adjacent 220 lot, 685 acre Thunder Ridge Development, (b) increase in building activity in the MEPOA service area as evidenced by the recent increase in new service connections to an annual level of 18, and (c) the continuing drought that has been occurring in Arizona. Thunder Ridge development is far from being completed, so pressure from that source could get worst. Information is not available to this writer (nor does he have the technical expertise) to determine how effective the current system is in meeting the peak demand of its 130 service connections. However a "back of the envelope" calculation utilizing the above current pumping rates and service connections indicates if the system were pumping 24/7, 365 days a year there would be just under six/tenths of an acre foot available on an

annual basis to each service connection. This availability appears to be on the low side of desirable, even before considering how practical it is to assume pumping at full capacity 24 hours a day, 365 days a year. The applicant acknowledges the situation and indicate they have investigated a possible source of additional water supply that they estimate can be acquired for \$12,000 plus an additional \$5,000 in development work to put the well in service. I don't believe the applicant indicated the anticipated pumping capacity of the well and perhaps it is not available as additional development work is required. In summary, it is obvious there should be concern about the system's capacity and it appears it could be a relatively expensive matter to resolve which would require a financial strong party.

As to meeting the new arsenic level regulations which become effective in January, 2006, MRWC has indicated they are considering the system tested at Black Canyon, which is a type of reverse osmosis (R/O) filtering system that is installed at each homeowner's residential water connection. At an October 14, 2004 MEPOA public meeting concerning the features of this system I believe it was stated this type of system requires the water provider to perform 3 on site maintenance procedures per year, 2 tests at 6 month intervals to determine if the system is functioning, and one annual change of the filter. From a layman's standpoint, assuming MEPOA's present connection count, it seems that there would be 130 points where this type of R/O system could malfunction. This compares to one possible malfunctioning source utilizing a central arsenic treatment plant where the water is brought to acceptable arsenic levels at the wellhead or a central distribution point. From the aspect of public health, I would suspect that a central arsenic treatment plant would be checking arsenic levels more frequently than once each six months. Additionally the water provider would be required to perform a significant number of maintenance service calls on the R/O type systems each year. At a minimum, assuming the present connection count, and that both a functioning check and filter change could be combined in one visit the water provider would be required to provide a minimum of 260 on site service visits each year. Making arrangements to gain access to a residence to do maintenance checks could be a hassle to the water company. At the same time, the periodic maintenance checks could be a problem for the homeowner who wants/needs to be at their home to provide access for a serviceman. With the number of two earner/single family situations prevalent in today's society, where no one is home during the working day, there could be numerous times where a MEPOA home owner will miss a day's pay to be present to provide access to a serviceman. My understanding is the initial cost of a central arsenic treatment plant is greater than the type of R/O system being considered by the applicant. However it seems it would be prudent to consider both the risk to public health and the maintenance costs of servicing multiple individual on customer site R/O systems in deciding which system is better in the long run for the MEPOA service area. Regardless of which type of arsenic treatment system is used a financial strong party will be required to implement the system.

The effectiveness of MEPOA's Board in seeking out a qualified financially sound buyer for its water system would be questioned by any reasonable observer. I have heard two

"History of the Water Company" presentations made by long time area residents. In both cases the parties mentioned that twice (the last time in 1999) in MEPOA's 20 year operating history Arizona Water Company (AWC), who owns the Rimrock water system adjacent to MEPOA's service area, has been approached for assistance/advice on the MEPOA water system and to see if AWC had any interest in acquiring/or taking the system over. In an April, 1999 letter, AWC indicated that due to MEPOA's water supply arsenic levels and the then water supply capacity of their Rimrock system they were not interested in acquiring MEPOA's system. **However, in the same letter AWC indicated that when additional water supplies were available in their Rimrock system they would like to renew discussions on the possibility of AWC providing water service to Montezuma Estates.** In the January 9, 2004 MEPOA meeting with property owners to discuss the vote on the impending sale to MRWC, I asked the question if any effort had been made to market the system to one of the area's established water companies. The reply from the MEPOA President was that no one but MRWC was interested in acquiring the system. Later in January, I contacted Lee Hetrick, Superintendent of AWC's Sedona office and learned they would be open to evaluating if MEPOA's could be combined into their Rimrock system, and based on the results of that evaluation entering into negotiations to acquire the MEPOA system. It is difficult to understand why MEPOA's Board did not make the same contact with AWC, especially since MEPOA had contacted AWC before, and **it was a matter of common knowledge in the community that AWC's Rimrock operations had recently developed a well with significant capacity.**

At the July 8th ACC hearing, MEPOA was requested to obtain a "letter from, some sort of communication from Arizona Water with respect to their interest in the utility, if any". Presumably based on a contact made by MEPOA management, William M. Garfield, President of AWC, furnished an August 5, 2004 letter to ACC in which he indicated "The Company is interested in pursuing the acquisition of the Montezuma Estates water system if the Association is also interested." The ACC furnished AWC's letter of interest to the parties involved with the application on August 12, 2004. On September 29, 2004, I contacted Mr. Garfield and asked how the evaluation and acquisition of MEPOA's water system was proceeding. He told me that AWC did not yet have the acquisition evaluation information they had requested from MEPOA. Concerned with the amount of time that passed without AWC being able to obtain that information, I contacted Douglas C. Fitzpatrick, MEPOA's attorney that day and asked him to follow up on expediting the furnishing of the necessary information to AWC. Mr. Fitzpatrick advised me on October 11, 2004 that this had been done. **Given MEPOA's delay in providing information to AWC, it can be questioned whether AWC will have adequate time to evaluate MEPOA's operation and develop a firm acquisition offer before the next scheduled application hearing date of October 28, 2004.**

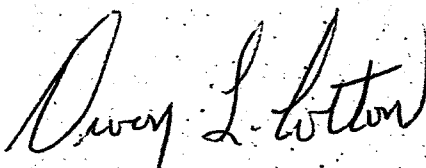
MEPOA's Volunteer Board has done a decent job, given the circumstances, for a long time of coping with the difficult situation of providing water service to the community while utilizing primarily a volunteer work force. However, the property owner's in MEPOA's service area should have the opportunity to be served by an established company such as AWC. AWC began doing

business in Arizona in 1955, and currently operates water systems in 18 communities throughout the state. The size of this operation allows them to have the engineering, operational, financial, and legal expertise and capacity to deal with the many technical and operating challenges involved with something as important as providing safe, abundant water supplies to rural residential and commercial customers. Having AWC as a water supplier could be a significant factor in improving the quality of life in the MEPOA community as well as providing a better base for developing the infrastructure necessary to handle the rapid growth and building activity that is presently occurring (and could likely continue) in the MEPOA service area. It would be unfortunate for MEPOA homeowners if the family relationships that exist between the individuals on the MEPOA Board and the person owning MRWC, the applicant, resulted in rejecting a water system buyer other than MRWC. A substantial buyer such as AWC, who has adequate water supplies to serve its own, as well as MEPOA'S service area, and an effective long term solution to the arsenic compliance requirements, should receive a prompt response to requests for information and an unbiased consideration of any proposal made for the acquisition of MEPOA's system.

The financial stability of the buyer of the MEPOA water system is a very important issue. MRWC, the applicant is proposing acquiring the system with 20% equity, utilizing a bank loan secured by the water system, to finance the balance of the purchase price. In addition MRWC could be rather quickly faced with significant expenditures for the arsenic and water supply issues. The result is that MRWC is thinly capitalized for the business risks involved. In the event of a default on the acquisition loan, home owners in the service area could be dealing with the bank as an owner and operator of the system. That could be even a more difficult situation than the present one where MEPOA owns and operates the system and residents, at least in theory, have direct control over their water supplier. In the event, no acquisition offer is received from AWC, or an AWC offer is rejected by the Board in favor of the MRWC proposal, **the Commission must seriously consider the need for a significant performance bond or letter of credit from MRWC to guarantee the financial performance and related operating capabilities of the applicant.**

If you or those copied have any questions concerning the above, the best way to contact me is on my cell at (602)980-1644 or by email at cnsowen@qwest.net.

Very truly yours,



Owen L. Cotton

cc: See next page

A COPY of the foregoing letter to Jim Fisher of the Arizona Corporation Commission was mailed to the following parties on October 20, 2004:

Docket Control
Arizona Corporation Commission
1200 West Washington St.
Phoenix, Arizona 85007

David M. Roland, Legal Division
Arizona Corporation Commission
1200 West Washington St.
Phoenix, Arizona 85007

Douglas C. Fitzpatrick
49 Bell Rock Plaza
Sedona, Arizona 86351

Peter O. Sanchez
60 Ridgcrest Road
Sedona, Arizona 86351

Montezuma Rimrock Water Company, LLC
P. O. Box 10
Rimrock, Arizona 86335-0010

Patricia D. Arias
7209 West Windrose Drive
Peoria, Arizona 85381

Richard Rink
6601 N. Mountain View Drive
Paradise Valley, Arizona 85253